CENTRAL BANK OF TRINIDAD & TOBAGO

CONSOLIDATED PRUDENTIAL REPORTING GUIDELINE

FOR INSTITUTIONS LICENSED UNDER THE FINANCIAL INSTITUTIONS ACT, 2008

February 2010 (FINAL)

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1. INTRODUCTION

Consolidated prudential reporting refers to the reporting of capital adequacy and credit exposures on a consolidated basis. Consolidated reporting is required by a licensee or a financial holding company (FHC) under various sections of the Financial Institutions Act, 2008 (FIA). Section 9(4) requires that capital adequacy, solvency requirements and capital ratios apply on a consolidated basis; section 42(12) requires credit exposures to be applied on a consolidated basis and section 43(11) requires connected party exposures to be applied on a consolidated basis.

Similar to the reporting of consolidated financial statements, consolidated prudential reports combine the assets, liabilities and off-balance sheet positions of entities within the group structure and treat them as if they were a single financial entity. Unlike the reporting of consolidated financial statements however, consolidated prudential reports include conditions or prudential criteria to treat with excessive leveraging, gearing, unregulated institutions or related party transactions within the group.

For example, in determining the consolidated capital adequacy requirements for a banking group, a licensee or FHC will be required to deduct the capital required for the insurance holdings in the group and accordingly the assets of the insurance company would not be included in the calculation of risk weighted assets for the group. The rationale for this treatment can be found in section 3.2.2.

The required capital ratio on a consolidated basis is the same as that established on a solo basis, i.e. capital to risk weighted assets should be at least equal to 8%. Similarly, the limit for credit exposures and exposures to all connected parties on a consolidated basis is 25% of the group’s capital base, whilst the limit for exposure to a single connected party or connected party group is 10%.

2. PURPOSE AND SCOPE OF GUIDELINE

The Guideline is made in accordance with sections 10, 42(12) and 43(11) of the FIA and seeks to provide FHCs and licensees within a financial group with guidance for consolidated reporting of:

- Capital adequacy and capital ratios;
- Credit exposures; and
- Connected party exposures.

3. CONSOLIDATED CAPITAL POSITION

The following steps are necessary in calculating the consolidated capital position of the group:

i. Determine the group structure – that is, the domain of consolidation within a group;
ii. Determine the scope of consolidation – this process identifies all relevant companies that fall under the domain of consolidation;
iii. Decide on the methods to be used for consolidation within the group for prudential capital purposes i.e. full consolidation, pro-rata consolidation or deduction;
iv. Calculate the capital base;
v. Calculate the risk weighted assets; and
vi. Calculate the capital adequacy ratio (capital base/risk assets) > or = 8%.

3.1 THE DOMAIN OF CONSOLIDATION

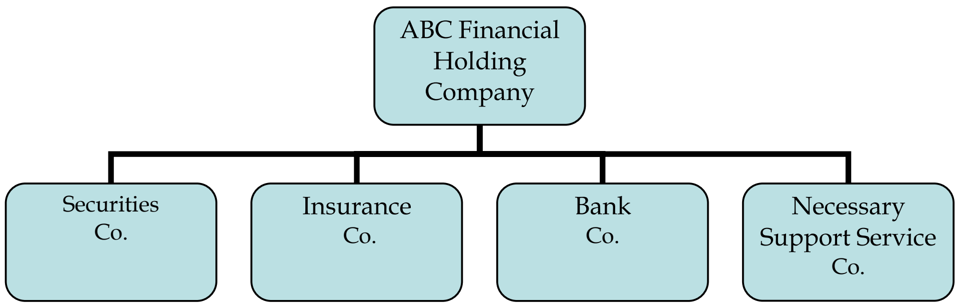
Group consolidation applies at the highest level of a licensee or FHC under the FIA. Consolidation will also apply at the level of a subgroup where the parent of the subgroup is itself a licensee or FHC.

The following illustrations present three scenarios or models of domain and the requisite levels at which consolidation will be required. Consolidation will be required where:

(a) The parent is a FHC

For Diagram A below, consolidation will be required at the level of ABC Financial Holding Company.

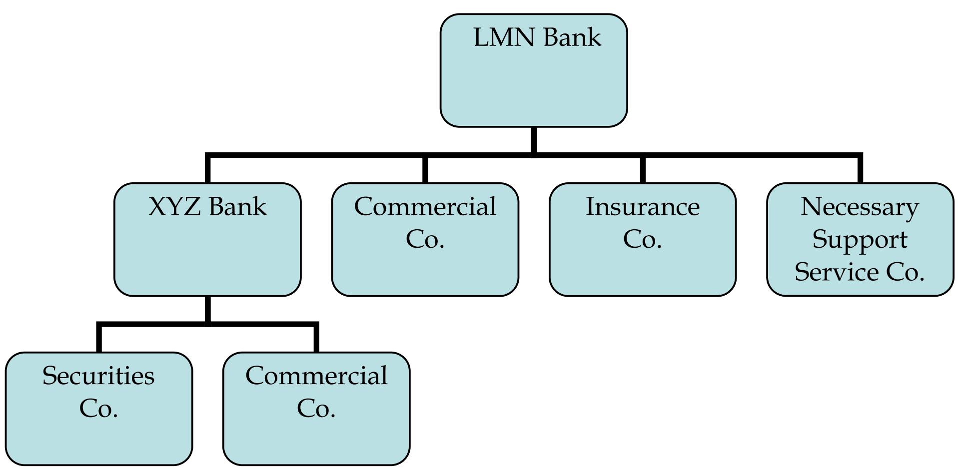
Diagram A



(b) A licensed financial institution (licensee) is a parent of a group of companies;

In Diagram B, consolidation will be required at the parent level of LMN Bank and will also be required at the sub-group level of XYZ Bank.

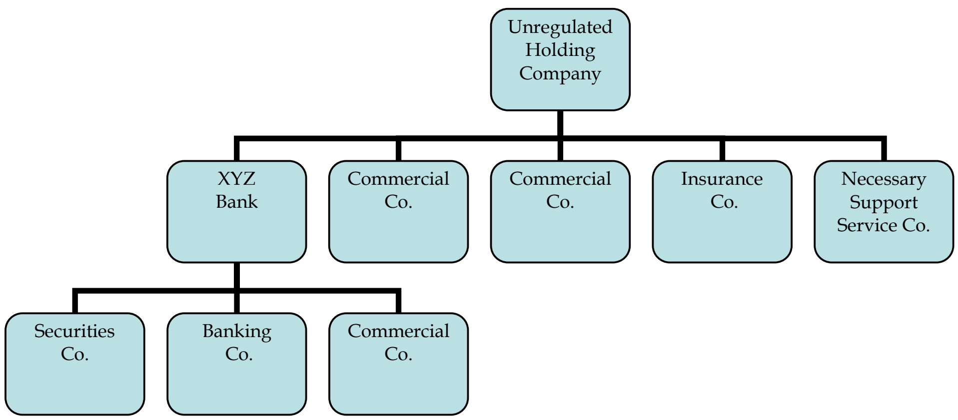
Diagram B



(c) The parent is not a regulated entity but has subsidiaries that are regulated then consolidation will apply at the sub-group level

In Diagram C, consolidation will be required at the sub-group level of XYZ Bank.

Diagram C



It is important to note that where in the preceding diagrams a licensee or FHC holds an unregulated subsidiary, the FIA requires that such entities be disposed of within three years after the coming into force of the FIA. Where the unregulated entity is providing a necessary support service that entity must be approved by the Central Bank.

3.2 SCOPE OF CONSOLIDATION

This section describes the types of entities that should be consolidated for the purposes of deriving capital adequacy reports. Based on international precedent and a review of practices in other jurisdictions, such entities would include:

- Licensed or regulated financial entities that are subject to prudential regulations in their home jurisdictions. Such financial entities include banks, merchant banks, investment firms, trust companies, securities firms, brokerages, and other financial institutions but exclude insurance companies;

- Unregulated financial entities that are not subject to solvency-based or other prudential requirements;
- Money transmission services; and
- Institutions that provide ‘necessary support services’[1]. Such institutions would include any undertaking where the principal activity consists of project financing, managing data processing services, providing advice and services relating to industrial strategy, mergers and the purchasing of undertakings or any other similar activity which is ancillary to the principal activity of one or more licensee.

3.2.1 Exclusions

A licensee or FHC may be required to exclude a subsidiary or participation from its consolidated prudential reports, where:

(a) inclusion would be inappropriate or misleading.

(b) the companies which otherwise would be consolidated have a combined balance sheet total of less than 1% of the balance sheet of the parent. The *de minimis* exemption may only be made for a number of companies, if the sum of their balance sheets meets the numerical test, otherwise they must all be included in the consolidated reporting.

(c) there are legal impediments to the transfer of information.

In addition to the exclusions described above, it may not be feasible or desirable for a licensee or FHC to consolidate certain securities and other financial entities for prudential capital purposes. In such circumstances, licensees or FHCs would be required to provide the Central Bank with evidence that such holdings are:

- acquired through previously contracted debt or underwriting of a share issue and are held on a temporary basis in the ordinary course of business; or
- subject to materially different regulation; or
- subject to non-consolidation for prudential capital purposes, by law.

[1] Reference section 41(3)(f) of the FIA.

3.2.2 Other Exclusions

(a) Insurance Holding Company;
(b) Insurance Companies;
(c) Insurance Brokers; and
(d) Real Estate Agencies.

With respect to (a) to (c) above, the primary risk that arises from the activity of insurance companies and insurance holding companies is insurance risk. Therefore, including this risk, which is unique for insurance companies, would not provide a meaningful determination of consolidated capital adequacy for the licensee or FHC in a financial group. Therefore, the capital investment in an insurance company (holding company or broker) is deducted from consolidated capital and its assets are not included in the group's risk weighted assets.

It should be noted that insurance companies will become subject to regulatory capital requirements under the revised insurance legislation and would be required to be adequately capitalized in accordance with the Insurance Act. Any capital deficits arising from the insurance holdings of a financial group must be deducted when calculating the consolidated capital requirement for the licensee or FHC at the top of the financial group or sub-group.

Regarding (d) above, a licensee or FHC is prohibited from acquiring or holding land or interest in land and therefore real estate agencies should not be part of a financial group (see section 41(3)(b) of the FIA). Consequently, where investments in real estate agencies exist, such investments must be deducted when deriving the consolidated capital position of the licensee or FHC.

3.3 METHODS OF CONSOLIDATION

The main methods or techniques of consolidation to be followed where applicable are full consolidation, pro rata consolidation and deduction[2].

[2] See definitions of full consolidation, pro rata consolidation and deduction in Appendix II.

3.3.1 Treatment of Financial Entities

(a) For participations of less than 20%, the entity's capital should be deducted from the group's capital base. The assets of such an entity are not included in the calculation of risk weighted assets for the group.
(b) Pro-rata consolidation should be applied for participations greater than or equal to 20% but less than or equal to 50%.
(c) Full consolidation should be applied for participations greater than 50% or where the licensee or FHC exercises control over the financial entity. (see definition of 'control' in the FIA.)

In cases where pro-rata consolidation should be applied to a financial entity, the Central Bank retains the discretion to require full consolidation of the entity, where it is deemed necessary. The following are some examples where the Central Bank may require full consolidation:

- If it is determined that the entity is wholly dependent on the parent for support:
- Where the FHC or licensee holds 50% of the shares of the financial entity and the remaining shares are widely held or are held by unregulated entities.

3.3.2 Treatment of Non-Financial (Commercial) Entities

(a) For participations of 20% or less where the entity does not fit the definition of a necessary support service, risk weighting is recommended. However, where the aggregate amount of all such investments exceeds a threshold of 60% of the group's capital, the amount of capital above the aggregate threshold is to be deducted from the group's capital base and its assets are not to be included in the group risk weighted assets.
(b) For participations of greater than 20%, the entity's capital should be deducted from the group's capital base and its assets are not to be included in the group risk weighted assets.

3.3.3 Unregulated Financial Entities

(a) For participations of less than 20%, risk weighting should be applied.

(b) Pro-rata consolidation will be applied for participations greater than or equal to 20% but less than or equal to 50%.

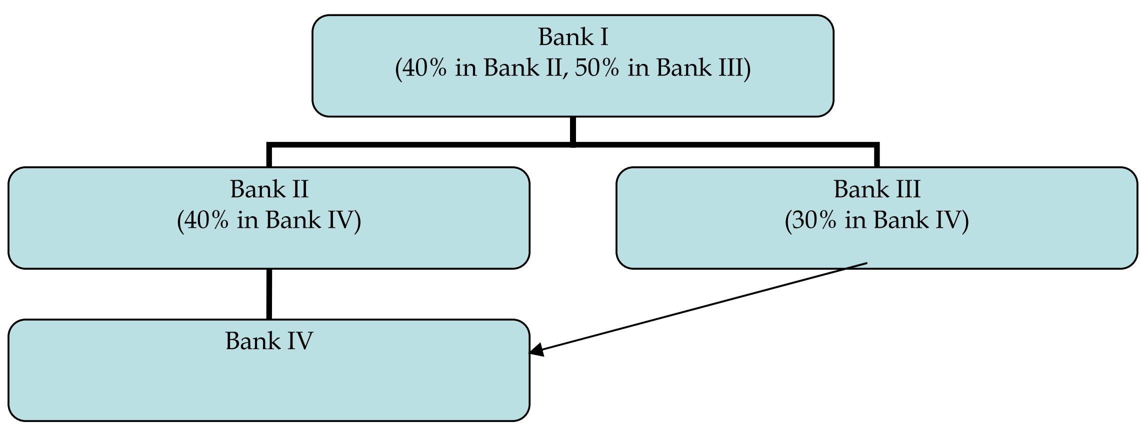
(c) Full consolidation will be applied for participation greater than 50% or where the licensee or FHC exercises control over the unregulated financial entity.

3.3.4 Cross-Shareholdings

If several entities within a group have participations in another entity within the group, then all indirect participations will be added to determine whether pro-rata or full consolidation would apply.

In Diagram D below, consolidation is required at the level of Bank I. Bank I has an indirect participation of 16% (40%*40%) in Bank IV via Bank II and also 15% (50%*30%) in Bank IV via Bank III. Total participation is 31% (16%+15%) thus pro-rata consolidation will be applied to Bank IV.

Diagram D



4. CONSOLIDATED CREDIT EXPOSURES AND CONNECTED PARTY EXPOSURES

4.1 Consolidated Credit Exposures

FHCs as well as licensees that hold subsidiaries are required to adhere to the credit exposure limits in Section 42 of the FIA on a consolidated basis. This means that the aggregate credit exposure of the group to a person, borrower group or related group must not exceed 25% of the consolidated capital base of the group as determined under the section "Methods of Consolidation".

Additionally, the aggregate principal amount of all such "large exposures"[3] of the group must not exceed 800% of the consolidated capital base.

4.2 Connected Party Exposures

Similarly, the credit exposure limits in Section 43 of the FIA for connected parties, are applicable on a consolidated basis to FHCs and to licensees that have subsidiaries. This means that the aggregate credit exposure of the group under the FHC or licensee to any one connected party or connected party group must not exceed 10% of the consolidated capital base.

Further, the aggregate principal amount of credit exposure to all connected parties and connected party groups must not exceed 25% of the consolidated capital base of the group.

4.3 Consolidated CB20 and CB40 Returns

In accordance with Section 75 (2), the reporting requirements of Section 75(1) which are normally captured in CB20 and CB40 returns, will apply on a consolidated basis to FHCs and to licensees which hold subsidiaries. Accordingly, FHCs and licensees to

[3] See Glossary for definition of "large exposure"

whom consolidated reporting requirements apply will be advised in due course of the details for submission of consolidated CB20 and CB40 returns.

5. REPORTING FORMS

All licensees and FHCs reporting on a consolidated basis will be required to complete a Consolidated Capital Adequacy Return on a quarterly basis. At present, this return is comprised of CB100A and CB100B Reporting forms. Forms to capture consolidated market risk positions will be incorporated in the return at a later date. The CB100A form requires licensees and FHCs to list all companies within the group and the total capital held by each company, in order to produce a final consolidated capital figure for the group. All licensees reporting on a consolidated basis are required to use the rules expounded in section 3 of this Guideline, in determining whether the capital for members of the group should be deducted, pro-rated or consolidated in full.

5.1 Completing the CB100A Form

The first item to be entered is the 'Name of Group' in cell B1. Cell A7 will be automatically updated with the name of the group from cell B1. All entities within the group must be entered within cells A8 to A57. Once this is done, the corresponding cells C6 to AZ6 will be automatically filled. All entities within the group should be entered whether they are to be included in the consolidated capital reporting or not.

FORM CB100A

	A	B	C	D	E	AY	AZ	BA	BB	BC
1	NAME OF GROUP:									
2										
6	COMPANIES WITHIN GROUP	CAPITAL						TOTAL CAPITAL POSITIONS	TOTAL PARTICIPATIONS IN THE GROUP	CONSOLIDATED CAPITAL
7	0									-
8										-
9										-
10										-
11										-
12										-
13										-
14										-
15										-
16										-
17										-
18										-
19										-
20										-
48										-
49										-
50										-
51										-
52										-
53										-
54										-
55										-
56										-
57										-
58								-	-	-

Under the second column, 'CAPITAL', the total shareholders' equity (per thousand) of the individual companies should be entered as they would appear in the balance sheet. In computing total shareholders' equity, audited retained earnings are to be used. The next set of columns, following the 'CAPITAL' column, is to be used to enter the book value of participations within the group (per thousand). Where there is goodwill, that is, the book value is greater than the capital in any entity, the goodwill must be deducted and the adjusted book value entered in this column.

For the column titled 'TOTAL CAPITAL POSITIONS', the capital positions (per thousand) derived using the methods of consolidation discussed earlier are to be placed in this column. No data needs to be entered in the final column titled 'CONSOLIDATED CAPITAL' as the column contains a formula which calculates the consolidated capital with respect to each company. This is found by subtracting the total of the participations from the total capital positions.

The consolidated group capital is found in cell BC58.

It should be noted that the risk assets of the group should be calculated using the same principles for the calculation of the capital base. That is, for full consolidation, risk assets are aggregated and where pro-rata consolidation is used, the relevant proportion of the risk assets should be included.

The consolidated capital adequacy ratio is similar to the capital adequacy ratio of individual licensees, that is, capital base divided by risk weighted assets should be greater than or equal to 8%. Additionally, consolidated Core or Tier 1[4] capital to consolidated risk adjusted assets should be greater than or equal to 4%.

5.2 Reconciliations

The consolidated capital figure in the CB100A tab should match the total qualifying capital on the CB100B tab. However, there may be instances where the capital figure in the CB100A and the CB100B do not match due to the differences in the components of capital allowed under the Basel framework, as compared to international accounting standards. For example, under the Basel framework:

1. Deferred tax is deducted from core capital and is currently captured in the CB100B form under line item #13 "Other Intangibles";
2. Subordinated term debt is allowed as a part of supplementary capital; and
3. A portion of general reserves/provisions for losses on assets is allowed as part of supplementary capital.

In instances where there are differences as outlined above, a reconciliation between the consolidated capital figure on the CB100A and the total qualifying capital figure on the CB100B should be submitted separately by the institution.

A worked example which applies the rules set out in Section 3 is shown in Appendix I.

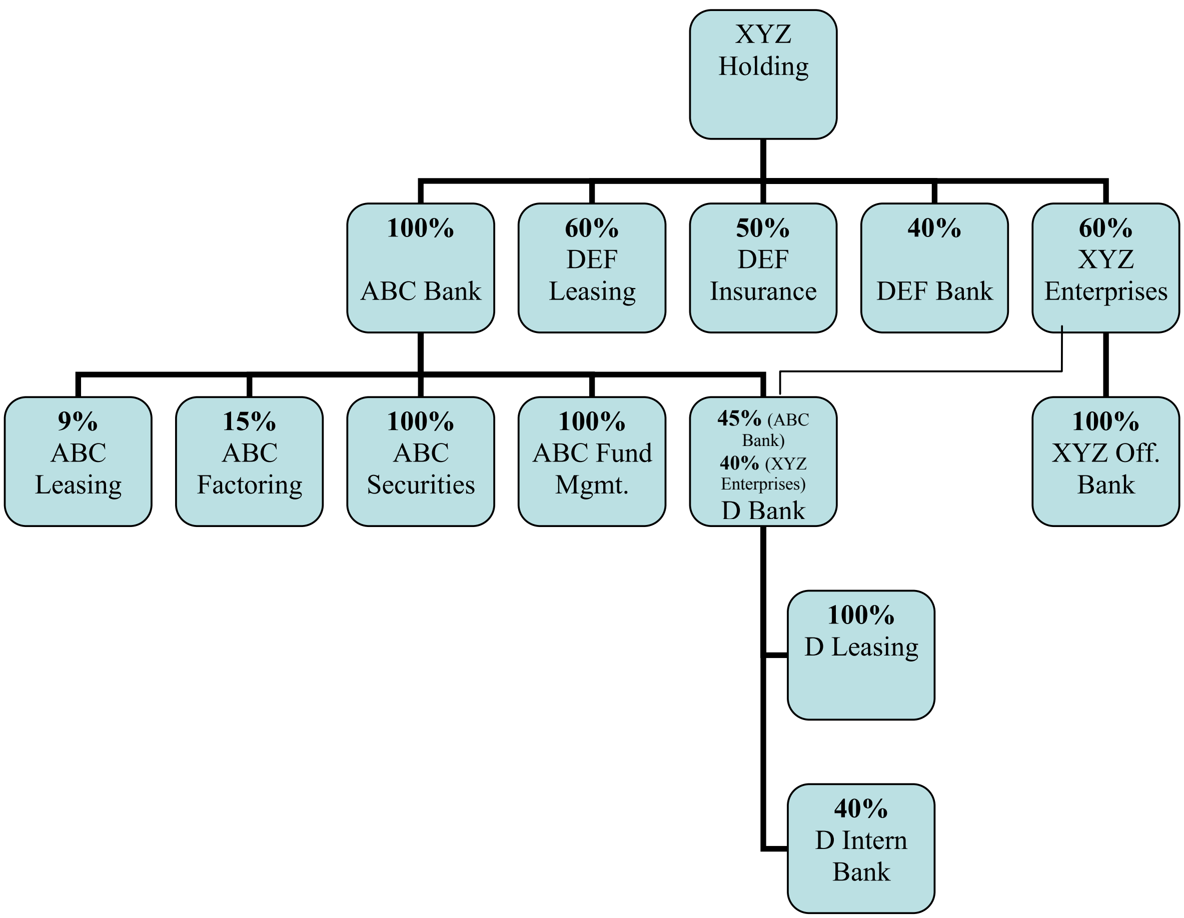
[4] Core or Tier 1 capital is the core measure of a bank's financial strength from a regulator's point of view. The composition of Core or Tier 1 capital is specified in the Financial Institutions (Prudential Criteria) Regulations, 1994.

APPENDIX I – AN EXAMPLE

Group Structure of the XYZ Holding Company

XYZ Holding has 600M in capital and invests 500M of its capital in its subsidiaries and associate companies, that is, ABC Bank, DEF Leasing, DEF Insurance, DEF Bank and XYZ Enterprises. The percentages in the diagram refer to the participations of XYZ Holding and its subsidiaries in the various companies within the group.

Diagram E



The following table reflects the capital for each member of the group and the capital to be consolidated. In this illustration, total consolidated capital for XYZ Holding is $882 million (See total of consolidated capital column).

		BOOK VALUE OF THE PARTICIPATIONS WITHIN THE XYZ GROUP															
	CAPITAL	ABC Bank	DEF Leasing	DEF Insurance	DEF Bank	XYZ Enterprises	ABC Leasing	ABC Factoring	ABC Securities	ABC Fund Mgmt	D Bank	XYZ O-Bank	D Leasing	D Int. Bank	**TOTAL CAPITAL POS.**	**TOTAL PART. IN GROUP**	**CONSOL CAPITAL**
XYZ Holding	**600**	100	100	100	100	100									600	500	**100**
ABC Bank	**125**						25	25	25	25	25				125	125	**0**
DEF Leasing	**250**														250		**250**
DEF Insurance	**220**														0		**0**
DEF Bank	**280**														112		**112**
XYZ Enterprises	**120**										25	95			120	120	**0**
ABC Leasing	**300**														0		**0**
ABC Factoring	**200**														0		**0**
ABC Securities	**30**														30		**30**
ABC Fund Mgmt	**30**														30		**30**
D Bank	**100**												15	15	100	30	**70**
XYZ O-Bank	**250**														250		**250**
D Leasing	**20**														20		**20**
D Int. Bank	**50**														20		**20**
	2575														1657	775	**882**

- The first column shows all the entities of the group (whether consolidated or not).
- The second column titled 'CAPITAL' shows the capital position of the individual companies as it would appear in the balance sheet.
- The next set of columns shows the book value of the participations within the XYZ Group. For example, ABC Bank has 125M in capital and invests 25M each in the companies ABC Leasing, ABC Factoring, ABC Securities, ABC Fund Mgmt and D Bank. The book value of a participation should normally be less than the capital of the subsidiary. There may be instances however, where the book value exceeds the capital position of the subsidiary. In such cases goodwill exists, which should be deducted.
- The column titled 'TOTAL CAPITAL POS.' uses the capital rules under the Section 'Methods of Consolidation' to apply capital consolidation. For example, XYZ Group has a 40% participation in DEF Bank, therefore pro-rata consolidation will apply. The capital position will be 112 = 40% * 280.
- The column titled 'TOTAL PART. IN GROUP' represents the total participations in the group. These participations are to be deducted from total capital positions to avoid double gearing of capital within the group.
- The final column represents the consolidated capital which is the difference between the total capital positions and the total of the participations.

APPENDIX II - GLOSSARY OF TERMS

deduction	the investment in the affiliate is deducted from the capital base. The assets of the affiliate are not included in the calculation of risk weighted assets.
full consolidation	means including in the group's consolidated returns all the relevant assets and liabilities of the companies being consolidated
pro-rata consolidation	means including in the group's consolidated returns only the group's share of the assets and liabilities in the affiliate concerned. Therefore, a company in which the group holds 25%, the capital adequacy returns would include 25% of that affiliate's capital, 25% of its assets and the large exposures returns would include 25% of its exposures.

Please see the FIA for definitions of the following terms:
affiliate, borrower group, connected party, connected party group, control, credit exposure, financial group, financial holding company, large exposure, licensee, related group, relative, significant shareholder, subsidiary